

Internal Revenue Service

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Person To Contact:
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Telephone Number:

Refer Reply To:
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Date:
January 18, 2012

Legend

Decedent =
Spouse =
A =
B =
C =
D =
Date 1 =
Date 2 =
Attorney =
State Statute =

Dear :

This letter responds to your letter dated June 21, 2011, requesting an extension of time under §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations to sever a trust pursuant to § 26.2654-1(b)(1) of the Generation-Skipping Transfer Tax Regulations and make an election under § 2652(a)(3) of the Internal Revenue Code.

Facts

Decedent died testate on Date 1 survived by Spouse, and A, B, C, and D. Spouse died on Date 2. C and D are skip persons, as defined in § 2613(a)(1).

In his will (Will), Decedent named Spouse as executrix of his estate. Decedent bequeathed all of his tangible personal property to Spouse and the remainder of his

estate to a trustee. The trustee was directed to fund two trusts, Marital Trust and Residuary Trust. Under Article IV of the Will, the trustee is to fund a trust with the minimum amount necessary to reduce Decedent's federal estate tax to zero by utilizing the marital deduction available (Marital Trust). Under Article V of the Will, the remaining assets will fund Residuary Trust.

Under the terms of Marital Trust, Spouse receives all income during her lifetime and principal distributions in the trustee's discretion for her health, education, support and maintenance. Upon her death, the trustee will distribute the corpus of Marital Trust to Residuary Trust. Under the terms of Residuary Trust, the trustee may make discretionary distributions of income and principal to Spouse during her lifetime for her health, education, support and maintenance. Upon Spouse's death, the trustee may make discretionary distributions of income and principal for the health, education, support and maintenance of A, B, C, and D. Upon the death of the survivor of A and B, Residuary Trust shall be divided into two separate shares and distributed outright to C and D, or their respective issue, per stirpes, if deceased.

Spouse hired Attorney to prepare the Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return. Attorney made a qualified terminable interest property (QTIP) election under § 2056(b)(7) with respect to the property in Marital Trust. In an affidavit, Attorney stated that he failed to advise Spouse that Marital Trust should be severed into a GST exempt QTIP trust and a GST nonexempt QTIP trust. Attorney also failed to advise Spouse that a reverse QTIP election under § 2652(a)(3) should be made with respect to the GST exempt Marital Trust, and that Decedent's GST exemption should be allocated to GST exempt Marital Trust. Upon the death of Spouse, the executors of Spouse's estate discovered that Marital Trust was not severed, a reverse QTIP election had not been made, and Decedent's GST exemption had not been allocated on Form 706.

The trust instrument does not provide for the severance of Marital Trust. However, State Statute authorizes a trustee to establish two or more separate trusts provided that such division will not materially impair the accomplishment of the trust purposes or the interests of any beneficiary.

To date, there have been no taxable terminations or taxable distributions from Marital Trust.

Requested Rulings

1. An extension of time under §§ 301.9100-1 and 301.9100-3 (1) to sever Marital Trust into two separate trusts on a fractional basis – one intended to be a GST exempt trust and the other a GST nonexempt trust – as permitted under § 26.2654-1(b)(1); and (2) to make a reverse QTIP election under § 2652(a)(3) with respect to the proposed GST exempt trust severed from Marital Trust; and

2. The automatic allocation rules of § 2632 apply to cause the unused portion of Decedent's GST exemption to be allocated to GST exempt Marital Trust.

Law and Analysis

Section 2001(a) imposes a tax on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2056(a) provides that, for purposes of the tax imposed by § 2001, the value of the taxable estate is determined by deducting from the value of the gross estate an amount equal to the value of any interest in property that passes or has passed from the decedent to the surviving spouse.

Under § 2056(b)(1), no deduction shall be allowed for an interest passing to the surviving spouse if, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, the interest will terminate or fail and (A) an interest in such property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than the surviving spouse (or the estate of such spouse); and (B) if by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse.

Section 2056(b)(7)(A) provides that, in the case of QTIP, the property shall be treated as passing to the surviving spouse for purposes of § 2056(a), and no part of the property shall be treated as passing to any person other than the surviving spouse for purposes of § 2056(b)(1)(A).

Section 2056(b)(7)(B)(i) defines "qualified terminable interest property" as property: (1) which passes from the decedent; (2) in which the surviving spouse has a qualifying income interest for life; and (3) to which an election under § 2056(b)(7)(B)(v) applies.

Section 2056(b)(7)(B)(v) provides that an election under § 2056(b)(7) with respect to any property shall be made by the executor on the return of tax imposed by § 2001. The election, once made, is irrevocable.

Under § 2044, any property in which the decedent had a qualifying income interest for life and for which a deduction was allowed under § 2056(b)(7) is includable in the decedent's gross estate.

Section 2601 imposes a tax on every generation-skipping transfer (GST).

Section 2631(a), as in effect on Date 1, provided that, for purposes of determining the GST tax, every individual shall be allowed a GST exemption of \$1,000,000 (adjusted for inflation) that may be allocated by such individual (or his executor) to any property with respect to which such individual is the transferor. Section 2631(b) provides that once an allocation of GST exemption is made, it is irrevocable.

Under § 2632(a), any allocation by an individual of his GST exemption may be made at any time on or before the date prescribed for filing the individual's estate tax return (including extensions).

Section 2632(c), as in effect on Date 1, provided that any portion of an individual's GST exemption which has not been allocated within the time prescribed by § 2632(a) shall be deemed to be allocated as follows - (A) first, to property which is the subject of a direct skip occurring at the individual's death, and (B) second, to trusts with respect to which the individual is the transferor and from which a taxable distribution or a taxable termination might occur at or after the individual's death.

Section 26.2632-1(d)(2) provides, in relevant part, that a decedent's unused GST exemption is automatically allocated on the due date for filing Form 706 to the extent not otherwise allocated by the decedent's executor on or before that date. Unused exemption is allocated pro rata (subject to the rules of § 26.2642-2(b)), on the basis of the value of the property as finally determined for estate tax purposes (chapter 11 value), first to direct skips treated as occurring at the transferor's death. The balance, if any, of unused GST exemption is allocated pro rata (subject to the rules of § 26.2642-2(b)) on the basis of the chapter 11 value of the nonexempt portion of the trust property to trusts with respect to which a taxable termination may occur or from which a taxable distribution may be made. However, no automatic allocation of GST exemption is made to a trust that will have a new transferor with respect to the entire trust prior to the occurrence of any GST with respect to the trust.

Under § 2652(a)(1) and § 26.2652-1(a)(1), the individual with respect to whom property was last subject to federal estate or gift tax is the transferor of that property for purposes of chapter 13.

Section 2652(a)(3) provides that in the case of any trust with respect to which a deduction is allowed to the decedent under § 2056(b)(7), the estate of the decedent may elect to treat all of the property in the trust for purposes of the GST tax as if the QTIP election had not been made. This election is referred to as the "reverse QTIP election." The consequence of a reverse QTIP election is that the decedent remains, for GST tax purposes, the transferor of the QTIP trust for which the election is made. As a result, the decedent's GST exemption may be allocated to the QTIP trust.

Section 26.2652-2(b) provides that the reverse QTIP election is to be made on

the return on which the QTIP election is made.

Section 26.2654-1(b)(1)(ii) provides, in part, that the severance of a trust that is included in the transferor's gross estate (or created under the transferor's will) into two or more trusts is recognized for purposes of chapter 13 if the governing instrument does not require or otherwise direct severance but the trust is severed pursuant to discretionary authority granted either under the governing instrument or under local law; and

(A) The terms of the new trusts provide in the aggregate for the same succession of interests and beneficiaries as are provided in the original trust;

(B) The severance occurs (or a reformation proceeding, if required, is commenced) prior to the date prescribed for filing the Federal estate tax return (including extensions actually granted) for the estate of the transferor; and

(C)(1) The new trusts are severed on a fractional basis. If severed on a fractional basis, the separate trusts need not be funded with a pro rata portion of each asset held by the undivided trust. The trusts may be funded on a nonpro rata basis provided funding is based on either the fair market value of the assets on the date of funding or in a manner that fairly reflects the net appreciation or depreciation in the value of the assets measured from the valuation date to the date of funding.

Sections 301.9100-1 through 301.9100-3 provide standards the Commissioner will use to determine whether to grant an extension of time to make a regulatory election.

Under § 301.9100-1(c), the Commissioner may grant a reasonable extension of time under the rules set forth in §§ 301.9100-2 and 301.9100-3 to make a regulatory election, or a statutory election (but no more than 6 months except in the case of a taxpayer who is abroad), under all subtitles of the Code except subtitles E, G, H, and I.

Section 301.9100-3(a) provides that requests for extensions of time for regulatory elections that do not meet the requirements of § 301.9100-2 must be made under the rules of § 301.9100-3. Requests for relief subject to § 301.9100-3 will be granted when the taxpayer provides the evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interests of the Government.

Section 301.9100-3(b)(1)(v) provides that a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer reasonably relied on a qualified tax

professional, including a tax professional employed by the taxpayer, and the tax professional failed to make, or advise the taxpayer to make, the election.

In this case, the executor of Decedent's estate made a QTIP election with respect to Marital Trust's assets, and Marital Trust's assets are includible in Spouse's gross estate under § 2044. Accordingly, Spouse is the transferor of Marital Trust's assets for GST tax purposes and the estate is precluded from allocating Decedent's GST exemption to Marital Trust's assets. However, if Decedent's estate is granted an extension of time pursuant to § 26.2654-1(b)(1) to sever Marital Trust into two trusts, a GST exempt trust and a GST nonexempt trust, and to make a reverse QTIP election under § 2652(a)(3) with respect to GST exempt Marital Trust, Decedent will be treated as the transferor of GST exempt Marital Trust's assets, and Decedent's GST exemption will be automatically allocated to GST exempt Marital Trust. It has been represented that Decedent has sufficient GST exemption to allocate to the GST exempt Marital Trust. The allocation will be effective as of the Decedent's date of death, Date 1.

Based on the facts submitted and the representations made, we conclude that the requirements of § 301.9100-3 and § 26.2654-1(b) have been satisfied. Accordingly, Decedent's estate is granted 120 days from the date of this letter to sever Marital Trust into a GST exempt trust and a GST nonexempt trust and to file a supplemental Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, on which the reverse QTIP election is to be made for the GST exempt trust. The automatic allocation rules will then apply to cause Decedent's unused GST exemption to be allocated to GST exempt Marital Trust. The supplemental Form 706 should be filed with the Internal Revenue Service Center, Cincinnati, Ohio 45999. A copy of this letter should be attached to the return.

Furthermore, except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed or implied regarding whether Marital Trust qualifies as a QTIP Trust under § 2056(b)(7).

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Associate Chief Counsel
(Passthroughs & Special Industries)

By: Leslie H. Finlow
Leslie H. Finlow, Senior Technician Reviewer
Branch 4
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures: Copy for § 6110 purposes
One copy of this letter